Chapter 14. Indonesia

Indonesia has traditionally adopted a social SME policy. Its most significant SME development programme is a financing scheme that enables its lower-income citizens to access capital, and this operates with rather low entry requirements. Many SME policies and programmes in Indonesia are implemented by local government authorities.
Overview

Economic structure and development priorities

Economic structure

Indonesia is ASEAN’s largest and most populous country, with a population of 258.7 million (ASEC, 2016) and a total land area of 1,913,579 km². Richly endowed in natural resources, it is home to substantial deposits of metals and minerals such as tin, copper, gold and nickel; coal; substantial oil and gas reserves; and it is also a major global producer of agricultural commodities such as rubber, palm oil and grains. As one of the three littoral states of the Strait of Malacca, it holds a strategic position over one of the world’s busiest shipping routes: by some estimates 40% of global trade passes through this channel every year. Largely due to these factors, it is the largest economy in ASEAN and the 16th largest economy globally, with a GDP of USD 932.3 billion in 2016 (World Bank, 2016a), and it is the only country in Southeast Asia to sit within the G20.

With a GNI per capita (PPP) of Intl$ 11,240, the fifth highest in the region, Indonesia is a lower middle-income economy. Economic growth has traditionally been driven by the country’s substantial natural resources, which still account for around 60% of exports. There is a large market for its commodities. Indonesia is the 24th largest export economy in the world, and its products are mainly absorbed by other Asian economies. China received 12% of exports in 2016, followed by Japan (11%) and Singapore (8%) (MIT,
In particular, it is the world’s largest producer of palm oil, and this is the country’s biggest export product, accounting for 10.2% of total exports in 2016. Yet the resource sector’s share of the economy has fallen since 2000 despite booming commodity prices. Economic growth since 2000 has instead been driven by labour productivity enhancements, particularly in the sectors of wholesale and retail trade; transport equipment and apparatus manufacturing; and transport and telecommunications. The economy is principally geared towards the domestic market, with private consumption the largest component of GDP expenditure. Yet production remains largely concentrated in low technology activities despite demand for high technology goods. High technology exports accounted for only 5.8% of Indonesia’s total manufactured exports in 2016, yet machines represent the largest category of its imports, accounting for 27% in 2016 (MIT, 2016).

The country has been undergoing a comprehensive process of reform to open up and liberalise the economy since the collapse of the Suharto government in 1998. It embarked upon this period of reform following a deep decline in output. Between 1998 and 2001 it enacted “big bang” decentralisation, which involved transferring most of the apparatus of government from the centre to the regions, implementing a new intergovernmental fiscal system and apportioning most of the public budget to regional governments. It has also established a strong macroeconomic framework since the Asian financial crisis in 1999, capping its annual budget deficit at 3%, and lowering its debt-to-GDP ratio from 100% in 1999 to 36.1% in 2015 (IMF, 2018). Vulnerabilities remain from long-standing issues surrounding tax collection. The country’s tax-to-GDP ratio is one the lowest in the region, standing at 11% in 2015, compared to an ASEAN average of 14%. The current presidency has committed to raising this ratio to 16% by 2019 (OECD, 2015), and has begun to implement a number of measures in this area. Public expenditure has been moderated through a substantial reduction of fuel subsidies in 2015; the subsidies amounted to around 3% of GDP in 2014 (IEA, 2016).

Table 14.1. Indonesia: Main macroeconomic indicators, 2012-2016

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Unit of measurement</th>
<th>Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP growth</td>
<td>Percent, y-o-y</td>
<td>6.0 5.6 5.0 4.8 5.0</td>
</tr>
<tr>
<td>Inflation</td>
<td>Percent, average</td>
<td>4.3 6.4 6.4 6.4 3.5</td>
</tr>
<tr>
<td>Government balance</td>
<td>Percent of GDP</td>
<td>-1.6 -2.2 -2.1 -2.5 -2.5</td>
</tr>
<tr>
<td>Current account balance</td>
<td>Percent of GDP</td>
<td>-2.7 -3.2 -3.1 -2.0 -1.8</td>
</tr>
<tr>
<td>Export of goods and services</td>
<td>Percent of GDP</td>
<td>24.6 23.9 23.6 21.1 19.1</td>
</tr>
<tr>
<td>Imports of goods and services</td>
<td>Percent of GDP</td>
<td>25.0 24.7 24.4 20.8 18.3</td>
</tr>
<tr>
<td>Net FDI (inflows)</td>
<td>Percent of GDP</td>
<td>2.3 2.6 2.8 2.3 0.4</td>
</tr>
<tr>
<td>External debt</td>
<td>Percent of GDP</td>
<td>28.3 30.0 34.0 37.0 N/A</td>
</tr>
<tr>
<td>Gross reserves</td>
<td>Percent of GDP</td>
<td>44.7 37.4 38.2 34.3 N/A</td>
</tr>
<tr>
<td>Domestic credit to the private sector</td>
<td>Percent of GDP</td>
<td>33.4 36.1 36.4 39.1 39.4</td>
</tr>
<tr>
<td>Unemployment</td>
<td>Percent of active population</td>
<td>6.1 6.2 5.9 6.0 5.6</td>
</tr>
<tr>
<td>GDP per capita</td>
<td>PPP (constant 2011 Intl$)</td>
<td>9 283 9 673 10 031 10 385 10 765</td>
</tr>
</tbody>
</table>


The main challenges for the Indonesian government will be to address a complex regulatory environment, insufficient infrastructure, uneven subnational resource distribution, and poverty and unemployment. As an archipelago nation with one of the world’s largest populations spread over around 6 000 inhabited islands, Indonesia faces a more challenging development task than many other countries. It has taken huge strides in poverty reduction, cutting poverty rates from 57.3% in 1990 to 6.8% by 2016. Yet
despite this impressive performance, around 17.6 million people in Indonesia remain poor, and the country continues to struggle with unemployment, particularly among young people. Though the rate has dropped in recent years, the share of those aged 15-24 classified as NEET (not in employment, education or training) was 21% in 2017 (ILO, 2017[7]), with a higher rate among women (27.5%, compared to 14.9% among men[9]). Achievement of the country’s target GDP growth rate of 7% over 20 years[6] is also hindered by inadequate infrastructure, which raises the investment required to expand output. Indonesia’s incremental capital-output ratio (ICOR)[8] is 5.7%, compared to a standard ratio of 3.0%, largely due to the lack of infrastructure, which drives up logistics costs for producers. Investment is also stymied by FDI restrictions in many primary and service sectors, and the country remains more restrictive to foreign investors than the OECD average or other ASEAN peers.[10]

Reform priorities

The government of Indonesia engages in medium- and long-term development planning under Article 4 of Law No. 25/2004 on National Development Planning. It is currently 13 years into its first long-term plan under this law, the National Long-Term Development Plan (RPJPN 2005-2025). The plan aims to build on the development goals outlined in the country’s 1945 constitution, which pledges to build a country that is developed and self-reliant, just and democratic, and peaceful and united. Its targets include reaching income per capita of approximately USD 6,000 (midway through the upper middle income threshold); reducing inequality; lowering poverty levels to under 5% of the total population; reaching food self-sufficiency; and guaranteeing that every household can access a stable and nutritious food supply. To achieve this, it aims to boost human resource development (particularly in STEM subjects); to enhance infrastructure; to encourage the expansion of a rule of law that is fair, consistent and non-discriminatory; to uphold state sovereignty; and to pursue a free and active foreign policy. It aims to transform the economy to realise an efficient mining and agricultural sector, a dynamic and competitive manufacturing industry, and a resilient service sector. Alongside this plan, the current presidency has outlined its own priorities, specifically 16 packages of deregulation measures that aim to make things much easier for businesses. Other flagship measures include the development of Indonesia’s maritime resources and infrastructure, particularly electrical power generation capacity. The inclusion agenda is also in view.

Four medium-term strategies are envisaged under the long-term development plan. The country is currently implementing the third of these, the National Medium-Term Development Plan 2015-19. The medium-term plan is implemented through annual government work plans, which become the basis for drafting the annual government budget. The current medium-term plan focuses on increasing the competitiveness of Indonesia’s commodity sector and boosting human resource development, particularly in advanced science and technology. It places particular emphasis on environmental measures, infrastructure development and reducing subnational disparities. The plan identifies challenges arising from a lack of investment, limited technology use, corruption, bureaucracy and subnational income and endowment disparities. To tackle these disparities, it aims to promote inclusive growth and labour-intensive investment, to provide more support for micro entrepreneurs, to develop social security for informal workers, to increase and widen access to basic services for the poor, to develop the agricultural sector and to stabilise inflation.
**Private sector development and enterprise structure**

**Business environment trends**

Indonesia’s market size, burgeoning internet and mobile phone penetration and good record of macroeconomic stability have made it an attractive place to do business. In 2017, FDI investment in Indonesia reached USD 32.3 billion, excluding investments in the banking and oil and gas sectors, an increase of 8.5% over the previous year. The country also has an active start-up scene, and is home to four of Southeast Asia’s seven unicorn start-ups.\(^{11}\)

The central government has implemented a number of reforms to improve the business environment since the last assessment. FDI growth can be attributed in part to a set of economic policy packages implemented between September 2015 and November 2016, known collectively as Jokowi’s Economic Package, after President Joko Widodo. This comprised 14 stimulus packages mainly focusing on deregulation, law enforcement and business certainty, interest rate tax cuts for exporters, energy tariff cuts for labour-intensive industries, tax incentives for investment in special economic zones and lowered tax rates on property acquired by local real estate investment trusts.

Private-sector activity continues to be hampered by limited infrastructure, corruption and issues surrounding bureaucratic efficiency as a result of big bang decentralisation (WEF, 2017\(^{[8]}\); World Bank, 2017\(^{[9]}\)). Steps could also be taken to improve basic health and education outcomes as well as labour market efficiency, which is affected by excessive redundancy costs, limited flexibility of wage determination and a limited representation of women in the labour force. The government has taken steps to address this constraint since the last assessment, for instance by passing Government Regulation No.78/2015 on Wages. This regulation introduced a new formula for provincial governments to calculate their local provincial minimum wage each year, with the intention of increasing clarity over annual minimum wage calculation in order to create a more certain business climate. The government is also seeking to attract more investment into infrastructure development by boosting government revenues and exploring new ways to tap into private and international financial institution (IFI) investment, such as blended finance.

Corruption remains prevalent in many areas, despite the best efforts of the Corruption Eradication Commission (KPK) and the Jokowi administration. Since 2015, the administration has been conducting a big push to bring public procurement and budgeting online, promoting e-governance as a key instrument to increase integrity. A number of other reforms have been enacted,\(^{12}\) but the presidential administration and the KPK face an uphill battle, with graft common in the judiciary, the police and the customs administration – the latter being an important obstacle to trading across borders. The KPK has achieved a number of big wins,\(^{13}\) but it also faces resource constraints, with lawmakers often threatening to cut funding. Promisingly, it has repaired relations with Indonesia's National Police and today the two share resources, with police officers on secondment constituting almost half of KPK’s staff. The KPK and the Jokowi administration also benefit from the support of Indonesian citizens, with anti-corruption remaining a popular rallying point.

**SME sector**

The number of SMEs in Indonesia is relatively opaque given the fact that sole proprietors, including subsistence farmers, are included in official SME statistics. Based on this definition, around 57.9 million enterprises were estimated to be operating in Indonesia in
2016, of which 99% (or 57.2 million) are classified as micro enterprises. Alongside these micro enterprises, there were estimated to be 645,222 small enterprises, 106 medium-sized enterprises and 5,066 large enterprises active in the country. The number of large enterprises is relatively low given the size of the economy, contrasting with 7,156 large enterprises in Thailand and 13,813 in Malaysia (2016). By the country’s definition, Indonesia appears to have a very high MSME density, with around 22.1 MSMEs per 100 people. The country also appears to have a high MSME density when a standardised OECD definition is applied (OECD, 2018).

Micro firms appear to demonstrate a high structural contribution to the Indonesian economy, but this is mainly due to the sheer numbers included in official SME statistics. In 2016, these enterprises accounted for 89% of employment and 10% of GDP. Despite the very low number of large enterprises, they contribute the most to GDP, accounting for 39% in 2016. By removing enterprises in the agricultural sector, it might be possible to get a clearer idea of MSME numbers. In this analysis, MSMEs account for 61% of GDP and 87.8% of employment, with micro enterprises contributing 10% of GDP and 58.4% of employment. Meanwhile they account for only around 15.7% of non-oil and gas exports (BPS statistics, 2013).

As in other countries, Indonesia’s MSMEs are concentrated in the wholesale and retail trade sector, which accounted for 46% of non-agricultural Indonesian MSMEs in 2016, followed by the manufacturing sector and hospitality and catering services, each representing 17% of the total. Geographically they are concentrated in Java, with the highest concentrations of non-agricultural MSMEs to be found in West Java (17%), East Java (17%) and Central Java (16%), representing 50% in total (BPS Statistics, 2015).

**SME policy**

Indonesia has traditionally taken a welfare approach to SME policy, regarding it as a tool to promote equity rather than efficiency. This approach, which resulted in a largely nationalist and socialist approach to economic development, has its roots in Indonesia’s colonial past and the needs that emerged after independence in 1949. In the period immediately following independence, economic policies largely focused on building up a national industrial economy around state-owned capital (i.e. state-owned enterprises, or SOEs). Measures to promote SME development predominantly focused on providing support to the country’s ethnic population (*pribumi*), who were regarded as facing competitive disadvantages relative to the other segments of the population, such as the country’s ethnic Chinese. Mohammad Hatta, one of the country’s chief pro-independence revolutionaries and its first vice president, promoted the country’s co-operative movement as a uniquely Indonesian tool for development, one that could pave a middle way between capitalism and socialism.

Despite steps to pivot away from the statist policies pursued under Sukarno, this approach was maintained under Suharto’s New Order reforms of 1966. It was based on the persistent notion that SMEs were mainly operated by *pribumi* (in contrast, for instance, to SOEs), and that the country’s *pribumi* were an economically weak group in society (Wie, 2006). Many measures to promote SME development under Suharto compounded this notion. For instance, under Article 50 of Indonesia’s Competition Law, small-scale enterprises are exempted from the law’s provisions based on an assumption that small-scale enterprises require protection from competition. Another example is the reservation scheme for small and micro firms, which excludes large and medium-sized enterprises from operating in certain sectors or subsectors unless they have established a partnership.
with a small or micro firm. Current MSME financing programmes have their roots in subsidy and mandatory lending programmes implemented under Suharto.

A slight pivot can be observed around 2007/8, with the formulation of SME policies that promote efficiency alongside equity considerations. These policies include the Policy to Accelerate the Development of the Real Sector and Empowerment of Micro, Small and Medium Enterprises (Presidential Instruction No. 6/2007) and Law No. 9/2018 on MSMEs, which currently underpins MSME strategies. The policies were formulated as part of a broader push to stimulate private sector development, but still propose a number of policy exemptions for MSMEs.

2018 ASPI results

**Strengthening the institutional, regulatory and operational environment (Dimensions 5 and 6)**

Indonesia retains a rather complex institutional, regulatory and operational environment for SME policy, which is perhaps not surprising in a country where policy makers must provide public services to a large and diffuse population. Its Dimension 5 score of 4.35 for SME policy framework reflects both the country’s long history of conducting SME policy and the observation that its approach to SME policy could be more strategic and better defined. The strongly social orientation of the country’s SME policy is understandable in a country with a more challenging developmental task than many other nations, but exploring new approaches, such as new organisational forms, and developing more robust mechanisms to assess policy and programme impact may be advisable over the long term. In the Dimension 6 area of legislation, regulation and tax, its score of 3.49 reflects the observation that Indonesia has been taking measures to reform regulations affecting the business environment in recent years, but that more could be done to ensure that this process is in the country’s long-term strategic interest, to inculcate the use of good regulatory practices in the development of regulations and to streamline platforms for transacting with the public sector.

**Framework for strategic planning, design and co-ordination of SME policy**

Indonesian law mandates the Ministry of Co-operatives and SMEs (MCSME) to co-ordinate SME policies, rather than an inter-ministerial council or committee. The MCSME has been in place since 2001, though the country has had a similar entity at the level of Directorate General in place for the past 50 years. As of 2014, MCSME had around 735 field staff spread over 33 provinces (populating 170 local units in total). It distributes funding to other implementation bodies, including local government agencies, and meets regularly with officials tasked with SME-related issues within the Ministry of National Development Planning (Bappenas), which is one of two ministries responsible for co-ordinating the country’s economic policies as a whole.

Policy design and implementation is performed by sectoral ministries in consultation with MCSME. There appear to be few mechanisms in place to monitor and evaluate the efficacy of SME policies and programmes. This governance structure may lend limited independence and flexibility (for instance over staff pay and organisational form, including integration of the private sector into its governance structure), and implementation bodies may have a rather narrow mandate that is strongly social in nature.

Since 2005, Indonesia has had a five-year strategic plan for SME policy. The current plan covers 2015-19 and has an implementation budget of IDR 1 677 trillion (Indonesian
rupiah). It was developed at the same time as the SAP SMED and the country’s National Medium-Term Development Plan (2015-2019), so its objectives are broadly aligned with the two. The plan seems to prioritise social policy over economic competitiveness objectives. This approach – viewing SMEs as a social group requiring assistance rather than a latent engine of economic growth – seems to have been pervasive among Indonesian policy makers since independence (Burger et al., 2015[13]). Mechanisms to monitor and evaluate implementation of the plan are limited. They mainly consist of reports to the Ministry of Finance on use of the budget and they rely on self-assessment. Surveys of participants and local implementers of SME development programmes suggest that many programmes are implemented without a thorough assessment of SME needs or full assurance of management quality (Burger et al., 2015[13]). Limited mechanisms to monitor and evaluate impact may compound this issue, resulting in an uneconomical use of public resources that persists over time.

Monitoring and evaluation of the strategy’s implementation is mostly conducted internally and assesses use of the policy’s budget rather than assessing impact. To inform MSME policies and their evaluation, statistics on the MSME population are available, but their coverage of sole proprietors, including in agriculture, inflates the population’s number, making it difficult to ascertain a clear picture of the country’s production structure. The data collection is generally conducted by the Central Board of Statistics through surveys and census.

Scope of SME policy

Indonesia has a legal SME definition that differentiates MSMEs by sales turnover and net assets. It does not include an employment criterion – generally a simpler criterion to capture, and thus used in countries that may face constraints in data collection. Perhaps for this reason, the legal SME definition is not used consistently throughout the public administration. The statistical agency BPS-Statistics exclusively uses an employment criterion, and the Financial Services Authority (OJK) also uses an alternative definition. The current legal definition is in the process of being amended; MCSME is implementing a memorandum of understanding with Bank Indonesia to include an employment criterion in the definition. The legal definition also does not clearly distinguish between cottage enterprises with little growth potential and SMEs, meaning that many government promotion policies are directed indiscriminately at an unmanageably large target group. Policy makers are aware of this constraint, but the welfare concerns of SME policy make this a politically sensitive topic in Indonesia.

Table 14.2. Indonesia’s SME definition

<table>
<thead>
<tr>
<th>Institution</th>
<th>Size classification</th>
<th>Indicator</th>
<th>Units</th>
</tr>
</thead>
<tbody>
<tr>
<td>Official definition of the government of Indonesia</td>
<td>Micro</td>
<td>Sales turnover</td>
<td>≤ 300 mln (USD 22,542)</td>
</tr>
<tr>
<td></td>
<td>Micro</td>
<td>Net assets</td>
<td>≤ 50 mln (USD 3,757)</td>
</tr>
<tr>
<td></td>
<td>Small</td>
<td>Sales turnover</td>
<td>&gt; 300 mln-2.5 bln (USD 22,542-187,857)</td>
</tr>
<tr>
<td></td>
<td>Small</td>
<td>Net assets</td>
<td>&gt; 50 mln-500 mln (USD 3,757-3,757,139)</td>
</tr>
<tr>
<td></td>
<td>Medium</td>
<td>Sales turnover</td>
<td>&gt; 2.5 bln-50 bln (USD 187,857-3,757,139)</td>
</tr>
<tr>
<td></td>
<td>Medium</td>
<td>Net assets</td>
<td>&gt; 500 mln-10 bln (USD 3,757-751,428)</td>
</tr>
<tr>
<td>BPS-Statistics (manufacturing sector)</td>
<td>Micro</td>
<td>Employees</td>
<td>1-4</td>
</tr>
<tr>
<td></td>
<td>Small</td>
<td>Employees</td>
<td>5-19</td>
</tr>
<tr>
<td></td>
<td>Medium</td>
<td>Employees</td>
<td>20-99</td>
</tr>
</tbody>
</table>

Note: World Bank official exchange rate (2016 average): USD 1 = IDR 13,308.
Source: Law No.20/2008 on Micro, Small, and Medium Enterprises; BPS-Statistics.
In defining the scope of SME policy, some countries include informal enterprises while others exclude them. In Indonesia, both formal and informal enterprises are included, based on Law No. 20/2008 on MSMEs. Studies suggest that the country’s informal economy is large. Estimates of total informal employment among the working population range from 51.9% to 72.5% (ILO, 2014[14]). Data suggest that informal workers are mainly in agriculture (50.6% in a surveyed sample), followed by the wholesale trade and hospitality sector (25.6%). These two sectors also employ the greatest share of workers informally compared to other sectors. According to the same survey, 88.4% of agricultural workers may be informal, followed by 67.3% of wholesale trade and hospitality workers. Informality is substantial in rural areas: 73.9% of rural workers may be informal, compared to 44.6% of urban workers (all data: BPS Statistics, 2015). Measures to reduce informality include the Kredit Usaha Rakyat (KUR) programme, which provides credit to MSMEs to informal enterprises (based on an understanding that limited finance is one of the main reasons for informality), and free business licenses for informal enterprises. However, this assistance may instead reduce incentives to formalise and may not be enough to increase productivity and growth.

Development of legislation and regulatory policies affecting SMEs

The process of developing and submitting new regulations and legislation is currently guided and governed by Law No. 12/2011 (on Making Rules). Public-private consultations are conducted, but not on a regular basis in the planning phase, and they generally take the form of formal consultations. SMEs are involved in this process, but only via associations and when they are directly affected by proposed regulation/legislation. There is no formal requirement that consultations take place, though a good practice handbook has been developed by Bappenas on how to conduct them. There is also no requirement to conduct regulatory impact analysis (RIA) in the development of new or the review of old regulations and legislation, though Bappenas has been attempting to socialise this practice since 2003. Currently RIA is used on an ad hoc basis, with no requirement to consider the potential impact on SMEs in the development of regulations and legislation. Rules that are introduced or reformed are listed on the website of the Ministry of Co-ordinating Economic Affairs, but the process does not appear to be accompanied by a proactive dissemination campaign to boost awareness of the rules, for instance via business associations.

Company registration and filing tax

Company registration and filing tax is rather burdensome in Indonesia. To be fully registered to operate, a limited liability company must complete more than ten procedures, taking more than 20 days and costing around 10.9% of income per capita. (World Bank, 2017a) The long time required to establish a business is mainly due to a requirement to register with, or obtain licenses from, a number of different government agencies, including the Ministry of Law and Human Rights, the Ministry of Trade, the Ministry of Manpower, the BPJS Ketenagakerjaan (a social security programme for employees), the BPJS Kesehatan (the mandatory national health insurance scheme) and the Tax Office. For instance, it takes seven days each to register with the social security and national health programmes, and in Surabaya registration with the Ministry of Manpower takes around 14 days. While a few of these procedures can in theory be completed online, in practice most of them also necessitate visiting government offices or notary publics. This can leave space for unethical practices. Registration with the local Ministry of Manpower office in Surabaya, for instance, is theoretically free of charge, but
in practice an unofficial administrative fee may be negotiated, usually starting at IDR 100,000.

A proprietor requires three company numbers in order to operate, trade and pay tax as a registered company in Indonesia: the TDP (the company registration certificate); the SIUP (to trade); and the NPWP (the tax identification number). A requirement that the proprietor reapply for the SIUP and the TDP every five years was repealed in 2017. However, in the case of the TDP, an active enterprise must still file a notification letter with the Company Registration Office; this is free of charge. These reforms should be a positive development for SMEs, since the previous requirements constituted an additional compliance barrier and required the payment of additional administration fees. Online company registration is now available throughout Indonesia, but the SIUP and TDP can be obtained after online company registration only in Jakarta and Surabaya, meaning that in practice online company registration is not yet fully operational. In order to register online, a would-be proprietor must first buy a registration voucher from Bank Nasional Indonesia (BNI) for IDR 100,000 and then request a company name and enter the voucher number on the website of the Directorate General Administration of General Law of the Ministry of Law and Human Rights. A bar code is then issued that must be notarised within 60 days. The entire process costs around IDR 1.6 million – equivalent to a month’s salary for minimum wage workers in some parts of Indonesia.16

E-government facilities

Policy makers can enhance the ease of complying with regulations through the development of e-government platforms. As in other countries, Indonesia is most advanced here in the area of tax. Online tax filing is possible through the website of the Tax Directorate General, and appears to be relatively well advanced. Pension and social security contributions can also be filed online, but both appear less advanced than the tax platform, and in the case of social security online filing is only available for the Jaminan Hari Tua scheme (a provident fund for private-sector workers). A unique identification number is available for online tax filing (the Electronic Filing Identification Number, or e-FIN), but there does not appear to be a unique identification number in place for other e-government transactions. The Ministry of Communication and Information recently started to adapt its Management Information Integration and Data Exchange (MANTRA) software into a portal for e-government services in order to facilitate data exchange between different government institutions. A few federal and regional government institutions have started to use this application. BPS-Statistics regularly conducts surveys on public satisfaction with e-government services.

Facilitating SME access to finance (Dimension 3)

Indonesia has been ranked 37th globally of 137 countries for financial sector development (third in the region after Singapore and Malaysia) (WEF, 2017[8]) and 55th of 190 economies for ease of getting credit (World Bank, 2017a[9]). It benefits from a strong macroeconomic environment, but has a low level of financial intermediation. Domestic credit to the private sector, a proxy measure of this, stood at 39.1% of GDP in 2015. Many individuals and enterprises are unbanked in Indonesia. Only 35.9% of the population aged 15 or older had a bank account in 2014. The country’s most substantial programme to catalyse SME financing is the KUR, which disbursed IDR 16.7 trillion (about USD 1.3 billion) over its first implementation period (2007-14), generating MSME loans worth around IDR 178.85 trillion (approximately USD 13.4 billion17).18 The country’s Dimension 3 score of 4.58 reflects the substantial work undertaken to increase
financial inclusion and the level of financial sector development in the country, but indicates that more can be done to strengthen the legal and institutional framework for extending finance, as well as monitoring and evaluating the performance of government schemes.

**Legal, regulatory and institutional framework**

Indonesia has mid-level framework conditions for supplying finance. Financial institutions are relatively able to assess and hedge against credit risk, and these conditions are rapidly improving. The country is currently developing a dual credit reporting system, spearheaded by OJK, the Financial Services Authority, following its incorporation in 2012. The dual system involves a new system, the Financial Information Service System (SLIK), and the existing system, which is based on a public credit registry and has been in place since 2006 (though a credit information facility has been in place since 1969). The credit registry, *Biro Informasi Kredit*, is managed by Bank Indonesia, and the OJK supplements this with a facility to encourage information exchange between banks, called the Debtor Information System (SID). This is now being supplemented by the new system, which from 2018 is managed by OJK directly. The registry currently covers less than 50% of the adult population and is not customised for MSMEs. It is hoped that the new SLIK facility, alongside the enactment of a new regulation to facilitate the establishment of private credit bureaus (Bank Indonesia Regulation No. 15/1/PBI/2013), will result in deeper and more accurate credit information coverage. Private credit bureaus are already arriving in Indonesia. The first, the Pefindo Biro Kredit, was established in 2015. These new bureaus offer to combine the data they extract from the SLIK with their proprietary algorithms to generate credit scores for individual borrowers. This should lower the costs for financial institutions of conducting credit assessment. In the World Bank’s latest *Doing Business* report, credit registry coverage had increased, following the implementation of these two reforms, to 55.3% from 51.8% the previous year, and credit bureau coverage to 18.3% from 0% the previous year (World Bank, 2017a).

In terms of the contracting environment, Indonesia has an adequately strong framework for creditor rights, scoring 6 out of 12 in *Doing Business* (World Bank, 2017a). In terms of enforcement rules, practices complicate out-of-court debt resolution (for instance, auction houses insisting that banks can only liquidate collateral with a court order). Loopholes in the country’s Bankruptcy Law also negatively affect creditor rights. For example, there is a clause whereby creditors can be prevented from enforcing their security interest for up to 270 days if the debtor obtains a debt moratorium, or 90 days if s/he is declared bankrupt. Both reduce the ability of Indonesian financial institutions to take security, and they push up collateral requirements for all firms. Policy makers and legislators are aware of the issue and are currently working to address it. In 2016, the Indonesian Supreme Court issued a circular that sought to clarify rules on the liquidation of collateral and out-of-court debt resolution procedures (Circular Letter No. 2/2016 regarding Enhancement of Efficiency and Transparency in Handling Bankruptcy and PKPU Cases in Court). There is also a lack of clarity over the perfection and priority of security interests. The law does not allow a firm to grant a non-possessory security right in the full breadth of its assets without requiring a specific description of the collateral, and secured creditors are not paid first when a firm defaults outside an insolvency procedure or when it is liquidated. The country does have an asset register in place for movable assets, and this is centralised, though it is not notice-based—a step that would increase the ease of registering, and registering interest in, a security. The country also
has a cadastre in place, with land ownership generally well covered and up to date. The system is only partially online, however, and more could be done to increase the cadastre’s coverage of rural areas.

In terms of equity financing, the country’s stock markets have further potential to grow. Stock market capitalisation stood at 42% of GDP in 2015, and there were two listed companies per 1 million people, compared to 87.3 in Singapore, for instance. The Indonesia Stock Exchange is currently developing a platform for small, high-growth firms called IDX Incubator, following approval by the OJK in 2017.

Sources of external finance for MSMEs

MSME lending is dominated by Bank Rakyat Indonesia (BRI), which accounted for 63% of all formal MSME lending in 2014. It has managed to dominate the market due to its long history and extensive network of branches that cover the breadth of the country, including rural villages. Its market position is strengthened by the fact that it is the biggest recipient of the KUR. Between 2009 and 2014, BRI disbursed 65% of the total KUR programme (World Bank, 2017b[15]). MSME loans accounted for around 17% of total outstanding commercial bank loans in 2017, though this is the dominant source of external finance for MSMEs. To stimulate bank lending to MSMEs, Indonesia has deployed two main policy tools: i) extension and expansion of the KUR (a repayment guarantee, which in its 2015 iteration also includes an interest rate subsidy component); and ii) a mandatory lending scheme, which has been in place since 2009 and instructs commercial banks to have allocated 20% of their total loan portfolio to MSME loans by 2018. The KUR combines a guarantee (previously 70%-80%, now to be negotiated between the scheme and partner banks) and an interest rate subsidy, capping interest rates on KUR-backed loans at 9%. Commentators have expressed concern that two elements of the new KUR programme – capped interest rates and the stipulation that enterprises can receive more than one KUR-backed loan – are likely substantially to increase the fiscal cost of the scheme for the government and to reduce its additionality over the long term (World Bank, 2017b[15]).

Table 14.3. Amendments to the KUR programme

<table>
<thead>
<tr>
<th>Feature</th>
<th>KUR 2007-15</th>
<th>KUR 2015-</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan size</td>
<td>Micro: up to IDR 20 mln</td>
<td>Micro: up to IDR 25 mln</td>
</tr>
<tr>
<td></td>
<td>Retail: IDR 20-500 mln</td>
<td>Retail: IDR 25-500 mln</td>
</tr>
<tr>
<td></td>
<td>Linkage: up to IDR 2 000 mln</td>
<td></td>
</tr>
<tr>
<td>Maximum effective interest rate (pa.)</td>
<td>Micro: 22%</td>
<td>Micro and Retail: 12% (2015); 9% (2016 onwards)</td>
</tr>
<tr>
<td></td>
<td>Retail: 14%</td>
<td></td>
</tr>
<tr>
<td>Maximum loan term</td>
<td>Investment capital: 5 years</td>
<td>Investment capital: 5 years</td>
</tr>
<tr>
<td></td>
<td>Working capital: 3 years</td>
<td>Working capital: 4 years</td>
</tr>
<tr>
<td>Guarantee share</td>
<td>Pari-passu 70% (general) or 80% (for priority sectors – e.g. agriculture and industry) on the outstanding amount plus interest, for banks with NPL below 5%; no portfolio cap; claim trigger: loan classified non-performing</td>
<td>Negotiated and agreed between banks and CGCs (Permenko 8/2015, Art. 9 (2))</td>
</tr>
<tr>
<td>Guarantee fees</td>
<td>Stipulated by government and paid to CGCs 2007-09: 1.50%</td>
<td>Negotiated and agreed between banks and CGCs, reportedly facilitated by KUR Committee, upfront 1.5% of loan amount</td>
</tr>
<tr>
<td></td>
<td>2010-14: 3.25% of guarantee</td>
<td></td>
</tr>
<tr>
<td>Interest rate subsidy</td>
<td>None</td>
<td>Micro: 10% of loan amount paid as subsidy</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Retail: 4.5% of loan amount paid as subsidy</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Interest rate subsidy calculated based on monthly outstanding amount and paid directly to bank, includes credit guarantee fee</td>
</tr>
</tbody>
</table>

Source: Co-ordinating Ministry for Economic Affairs of Indonesia, in World Bank (2017).
Collateral requirements appear to be high for MSME loans, ranging from 238.6% of the loan’s value for small firms and 253.1% for medium-sized firms, according to Enterprise Survey data (World Bank, 2015[16]). Indonesia also has 21 separate credit guarantee schemes in place, of which the three biggest are Askrindo, Jamkrindo and Jamkrida. Askrindo and Jamkrindo operate at the national level and Jamkrida (a network of regional companies funded by provincial governments) at the provincial level. The two largest entities are Askrindo and Jamkrindo, in line with a regulation that a guarantee company can only operate nationwide if it has minimum capital of IDR 100 billion. As of Q4 2016, these two schemes held assets amounting to IDR 10.8 trillion and IDR 13.8 trillion respectively, and operated in all provinces of Indonesia. Both institutions have a strong capitalisation profile and strong business position, but exhibit an operating performance that is moderated by high claims from the KUR programme (Pefindo, 2016a[17]; Pefindo, 2016b[18]). Both provide KUR guarantees to eligible banks, but neither currently monitors nor evaluates the additionality of the programme. Both are state-owned companies, falling under the jurisdiction of the Ministry of State-Owned Enterprises, and the minister is responsible for appointing the governance and supervisory boards of both companies, a feature that may reduce their independence and market orientation. All three are regulated by the OJK under Law No. 1/2016 (regarding Guarantee), which superseded other previous laws. The OJK is currently discussing the establishment of a Regional Credit Guarantee Company in four new cities: Medan, Manado, Jambi and Gorontalo.

Indonesia has an export financing scheme in place, which it provides through Indonesia Eximbank, a special financial institution established under Law No. 2/2009. It has a special facility in place that targets SMEs, the Export-Oriented People's Business Credit facility, which provides working capital and investment loans in both local and foreign currency. The scheme disbursed IDR 1 trillion (USD 75 million) in 2016.

Microfinance products are also available for MSMEs. There is a large but unknown number of microfinance institutions (MFIs) in Indonesia, with estimates varying from 40 000 to 600 000. They take the form of rural banks, or Bank Perkreditan Rakyat (BPR), estimated to number 1 643; co-operatives (188 181); and an unknown number of unlicensed BPRs, village-owned financial institutions (Badan Kredit Desas) and NGOs (KPMG, 2015[19]). The OJK has recently rolled out a series of measures aimed at increasing regulatory oversight of microfinance providers. In 2015 it enacted a Microfinance Law (Law No. 1/2013) coupled with an institution-mapping exercise. The law introduces new licensing requirements, prohibits foreign ownership of MFIs, limits MFI activities (for instance, it disallows insurance activities, foreign exchange, guarantees and loans to other MFIs) and introduces capital requirements and financial reporting standards. Since its enactment, informal MFIs have entered the formal financial system. The OJK also issued “branchless banking” rules that aim to increase microfinancing through Indonesia’s already extensive bank branch network. The new rules allow for simplified customer due diligence procedures at banks that fulfill certain criteria, aiming to reduce the volume of documentation required for obtaining an MSME loan. Both measures are expected to benefit commercial banks while disciplining smaller MFIs and wholesale MFI lending banks. Smaller MFIs will now need to obtain a license and become a legal corporation, which will impose costs. The Microfinance Law stipulates that MFIs serving villages and subdistricts must have minimum capital of IDR 50 million, while those operating at district levels must have a minimum of IDR 100 million – criteria that many MFIs will not meet (KPMG, 2015[19]).

A wide range of asset-based financing instruments are available in Indonesia. The volume of such products is relatively low, but it has been increasing over recent years due to high
growth in the broader economy and strong demand for transportation and infrastructure development. Leasing is the most commonly used asset-based instrument. In 2016, Indonesia counted 29 leasing and two factoring companies, and total factoring turnover amounted to EUR 682 million (compared to EUR 40.5 billion in Singapore), of which the majority (99.7%) was domestic (FCI, 2017). Asset-based financing instruments are mostly extended by multfinance companies, and these activities are regulated by the OJK. Few MSMEs have access to asset-based financing.

Equity-based instruments, meanwhile, are growing rapidly. The country scores 17th on the Global Competitiveness Index (GCI) on venture capital availability (third in ASEAN and above many OECD countries) (WEF, 2017), and for the last few years it has accounted for the second highest share of private equity/venture capital (PE/VC) deals in ASEAN, alongside Malaysia and after Singapore. Among equity-based instruments, venture capital dominates, and this is also the area with the strongest regulatory oversight. In 2015, the OJK passed a series of regulations to govern the industry that expanded the range of investment and exit options open to VC. As of 2016, there were 65 venture capital funds operating in Indonesia, with deals between 2015 and 2016 amounting to around IDR 13 trillion. The greatest number of deals were in the seed stage (43%, or around 21), while the majority of value belonged to late-stage (debt/private equity) investments (40%, or around USD 1.2 billion). Between 2012 and August 2017, 96% of these investments were in e-commerce (58%) and transport (38%). The majority of VC investment in 2017 originated from China, with Chinese investors accounting for 94% of the USD 3 billion raised between January and August 2017, relative to 2% in 2016. This was mainly due to three big investments in three Indonesia companies: GoJek (a ride-hailing company) raised USD 1.2 billion from Tencent, Tokopedia (an online marketplace) raised USD 1.1 billion from the Alibaba Group, and Traveloka (an online travel company) raised USD 500 million from JD.com (AT Kearney, 2017).

Enhancing access to market and internationalisation (Dimension 4)

Despite its large domestic market, Indonesia recognises the importance of exposing SMEs to larger potential trade partners and markets and has put considerable effort into promoting greater international market access and internationalisation for its SMEs. This is reflected in its high score of 5.25 for Dimension 4, indicating an advanced level of policy development.

Export promotion

Export promotion programmes in Indonesia, including those that support SMEs in particular, involve multiple ministries or agencies. Enhancing export promotion for SMEs is a goal of the Strategic Plan 2015-2019 of MCSME and the Co-ordinating Ministry of Economic Affairs. The Ministry of Trade, through the Directorate General for National Export Development (DGNED), acts as a main national export promotion agency, with several initiatives geared towards SMEs. Other entities that provide services to SMEs are the Ministry of Industry, the Export Funding Agency and business associations. They disseminate foreign-market intelligence and free trade orientation and facilitate the participation of SMEs in trade fairs, both domestic and international. The Ministry of Trade mandates that all export promotion programmes be based on citizen aspiration, and formal consultations with various stakeholders have been conducted in developing them.

Among DGNED initiatives are training sessions provided by the Centre for Export and Import Training, which aims to turn local SMEs into active exporters, and the Regional
Centre for Training Export Promotion, an export promotion office established in various provinces to reach SMEs throughout the country. Together with DGNED, MCSME also facilitates the participation of local SMEs in international trade fairs in order to expose them to opportunities to export. In 2017, MCSME facilitated the participation of 109 SMEs in international trade fairs, such as the Malaysia International Halal Showcase and Chibimart Summer in Italy (Trihendrawan, 2018[22]). DGNED also established the Indonesia Trade Promotion Centre (ITPC) and deployed trade attachés in major cities worldwide to promote the country’s exports, especially from SMEs. Today, ITPCs are present in 19 cities in 18 countries. As a non-profit government agency, DGNED provides all of its services free of charge.

To better reach SMEs across the country, DGNED also conducts regular national activities involving the participation of SMEs from all provinces and districts. Notable activities include Designer Dispatch Service, an annual SME product design competition co-ordinated by the Indonesia Design Development Centre in which districts propose local SME products with innovative design carrying local heritage identity to compete at the national level. The best products are further developed by product design experts and promoted as export commodities. Meanwhile, decentralisation has given Indonesia’s provinces and districts a certain autonomy to come up with, fund and implement their own development programmes, and many have introduced SME export support initiatives. For example, the Yogyakarta provincial government regularly holds Jogia Trade Expo, an annual export exhibition, to promote products from local export-oriented SMEs and to provide further financial and networking assistance for SMEs participating in the exhibition (Yulianingsih, 2015[23]). The central government (through implementing ministries) and local governments regularly monitor all programmes, and their annual reports are publicly available.

Integration to GVCs

Measures to promote integration into global value chains (GVCs) are relatively scarce in Indonesia, and the concept has only recently entered into the county’s strategic planning documents. In MCSME’s latest medium-term plan, one of the targets is to facilitate the integration of 6 000 co-operatives and SMEs into global supply chains.

Promoting SME integration into GVCs has mostly been initiated indirectly through foreign investment regulations. Presidential Decree No. 44/2016 (on Negative Investment List) identifies industries and sectors that are closed to foreign direct investment (FDI) unless in partnership with local SMEs. The government, through Law No. 25/2007 (on Capital Investment), also mandates investors to do business with SMEs. These regulations provide opportunities for SMEs to engage directly with multinational corporations (MNCs) and enter into GVCs. In addition, Government Regulation No. 17/2013 (on the Implementation of Law No. 20/2008 on SMEs) encourages large corporations to establish business linkages with SMEs and to promote technology and skills transfers. These regulations are implemented by various agencies.

Use of e-commerce

Indonesia has a clear legal framework on the promotion of e-commerce growth. Law No. 7/2014 (on Trade) regulates e-commerce practices, while the Bank of Indonesia’s Regulation No. 11/12/2009 (on Electronic Money) and Regulation No. 18/40/PBI/2016 (on the Implementation of Transaction Payment Process) deal with e-payments. Consumer protection issues are covered by Law No. 8/1999, while specific protection
issues on payment systems are regulated by Bank of Indonesia’s Regulation No. 16/1/PBI/2014.

Cross-ministerial initiatives to promote the use of e-commerce among SMEs include SMEs Go Online, a national programme under MCSME co-ordination that aims to facilitate the shift of 8 million SMEs towards the digital space by 2020. The programme, conducted with the Ministry of Communication and Information and provincial and district governments, targets SMEs in each district for help in using e-commerce platforms. MCSME has partnered with leading e-commerce companies such as Lazada, Shopee, Bukalapak and Tokopedia. In November 2017, CNN Indonesia reported, quoting the ministry, that the programme had helped 3.79 million SMEs to go online, or about 8% of all SMEs in Indonesia (Ayuwuragil, 2017[24]). To reach out to as many SMEs as possible across the country, MCSME has collaborated with local governments in implementing SMEs Go Online. For example, 206 000 local SMEs in Sidorajo district, East Java Province, were targeted to receive assistance under the programme in 2018, KeuanganLSM.com reported on 27 December 2017 (Yusuf, 2017[25]). Another key initiative is the Ministry of Communication and Information’s One Million Domain Names programme, which provides free, ready-to-use websites for SMEs and public communities (e.g. schools or health care providers). The government is also designing an e-commerce roadmap, in close consultation with private providers.

Quality standards

Helping SMEs to improve quality standards is a target of MCSME’s Strategic Plan 2015–2019. The ministry aims to help 10 000 SMEs meet various standards – ISO standards, Halal certification, Indonesian National Standards (SNI) – by 2019 in order to improve their competitiveness. Towards meeting this target, SMEs will get training and special discounts on the certification of their products or services. According to the ministry’s 2015 performance report, a budget of almost IDR 12 billion was allocated, of which nearly 90% was used on 1 000 SMEs involved in quality standard programmes. Work on Indonesian quality standards mainly falls under domain of National Standards Agency (BSN), which develops national standards, and the Indonesian Food and Drugs Administration (BPOM), which regulates the manufacture and distribution of food and drugs. In developing national standards, BSN always refers to international standards and best practices, such as International Organisation for Standardisation (ISO) standards and the World Trade Organisation (WTO) code of good practice. BSN represents Indonesia as a member body in ISO, and it partners with various international organisations such as WTO and the American Society for Testing and Materials. Halal certification falls under the jurisdiction of the Indonesian Ulema Council through its division of food, drugs and cosmetic assessment.

Initiatives to assist Indonesia’s SMEs with quality standards are multi-agency collaborations. BPOM provides training on food and cosmetics safety and free halal certification programmes for SMEs. Following the issuance of Minimum Service Standard regulations in 2010, particularly on education and health, more technical regulations were enacted by each ministry in charge of each type of service sector. For instance, the Tourism Ministry issued a law on quality certification in the tourism service. 22

With education and health services mainly under the government’s purview, service quality standards in other areas are handled by business associations and communities. For example, Indonesia Chartered Accountants develops accounting standards for
businesses, including specific standards for SMEs, in accordance with standards developed by International Financial Reporting Standards. BSN has developed specific quality management standards for SMEs in several sectors, such as construction and agriculture, to enhance SME competitiveness in key areas of economic development. Efforts to help SMEs comply with standards also have been decentralised to local governments. For example, the Central Java provincial government has established Quality Management Standard Clinics in co-operation with BSN to assist local SMEs in improving their management quality and getting SNI ISO 9001 certification, a national standard that adopts the ISO 9001 quality management system.

**Trade facilitation**

Indonesia received moderate scores in the 2017 OECD Trade Facilitation Indicators (TFI) covered in this 2018 ASPI. It scored highest on information availability and formalities procedures. Several SME-specific initiatives to facilitate trading across borders have emerged. The *Kemudahan Import Tujuan Ekspor* (KITE) programme, through the Indonesian Customs Office, waives import duties and taxes for exporting SMEs. The Ministry of Finance also appointed a special unit at the Customs and Excise Office as the facility agent at regional levels to assist SMEs. The Indonesian National Single Window, Inatrade, handles enquiries and acts as a trade portal for traders. Furthermore, for SMEs that use the single window, the DGNED offers support in the form of training and assistance with export document preparation and submission.

Under a Ministry of Finance regulation (No. 227/PMK.04/2014), volume traded is not a criterion for Authorised Economic Operator (AEO) status. This allows SMEs a greater chance to qualify as an AEO. However, the AEO programme has no other special treatment for SMEs. Activities that can help SMEs obtain AEO status are still mostly in the form of seminars and workshops conducted by the Directorate General of Custom and Excise. For example, a discussion session was held at the Jakarta International Logistic and Supply Expo (JILSE) Forum 2017. However, since an entity can qualify as an AEO only if it possesses several advanced management qualities (such as a trade system database that is auditable for customs purposes, a public accountant and a crisis management system), more concrete measures are needed for SMEs to be able to meet these requirements.

**Boosting productivity, innovation and adoption of new technologies (Dimension 1 and 2)**

Indonesia has increased efforts to boost MSME productivity, innovation and the adoption of new technologies over recent years, including in the area of MSME greening. Despite this progress, Indonesia’s innovation performance remains relatively weak compared to Southeast Asia’s frontier economies. It has not yet developed a technology-intensive industry structure, and imports of high-technology products outweigh exports. Based on available data, Indonesia’s gross expenditure on R&D (GERD) is less than 0.1% of GDP, and little private sector investment has come forward to fill the gap. Limited inputs are reflected in the country’s outputs: the number of patent applications and scientific and technical publications remains relatively small. Indonesia’s Dimension 1 score of 4.14 indicates that while most requisite policies are in place, further implementation work may be required to realise the impact of these policies. The situation is similar with SME greening. Although plans are in place, more could be done to move forward with implementation and providing special incentives for SMEs. Indonesia’s Dimension 2 score of 3.28 on SME greening puts it on a par with regional peers.
Productivity measures

Many Indonesian bodies are involved in productivity policy. Bappenas, the Ministry of National Planning, leads policy development for productivity enhancement among SMEs, while MCSME and the ministries of Labour and Industry lead the implementation of such policies and programmes. Meanwhile, the Directorate of Productivity Development (DPD) under the Ministry of Labour is responsible for overall national productivity. The DPD has productivity training centres in 22 provinces.

The MCSME Strategic Plan 2015-2019 includes elements on productivity enhancement, with an average growth target of 5%-7% each year until 2019. Elements for raising SME productivity are included in SME development programmes in areas such as production capacity; access to market and finance; human capital development; institutions; and business environment in general. There are also specific programmes on productivity enhancement for micro enterprises and co-operatives, including one on strengthening business systems and technology through 1 000 technopreneurs until 2019. Members of the National Productivity Board are consulted on the development of programmes and policies with representatives from 17 ministries, labour unions, employers’ associations and universities. Public-private dialogues on productivity are conducted by the Ministry of Industry (MoI) every six months. Training sessions and workshops are often conducted with support from donors, including the Asian Productivity Organisation. Recently, there have been changes within the structure of the Ministry of Manpower and Transmigration (MPT) that negatively affected the performance of the DPD. Furthermore, recent budget cuts have affected the performance of productivity enhancement programmes. At the national level, the DPD monitors labour productivity by sector and geographical location annually in co-operation with the National Statistical Agency. However, data on other key performance indicators (KPIs), such as total factor productivity, are still limited. MCSME stands as the lead monitoring agency of its own SME productivity enhancement programmes.

Business development services

Indonesia has been providing business development services (BDS) to SMEs for over 15 years and it has a dedicated policy framework for this. Although MCSME is seen as a co-ordination body, BDS have been decentralised since early 2000 and vary across provinces. The MCSME Strategic Plan 2015-2019 covers BDS, with a range of programmes and initiatives.

The flagship initiative for BDS is implemented through centres for integrated commercial services, called PLUT (Posit Layanan Usaha Terpadu), which operate at the provincial level. In 2014-2016, a total of 192 850 companies received assistance from these centres. Currently there are 51 PLUT centres spread across 32 provinces. There is also a concept for developing PLUT at a national level. Generally each PLUT employs five to seven support staff who also provide capacity building on business management, access to finance, networking and accounting. The centres do not provide support with innovation or technology transfer, nor have they provided customised support. However, SMEs have access to mentoring services conducted by independently recruited consultants. Although customised BDS are currently available only in Sukabumi, in 2017 the government took a large-scale initiative to support SME scaling with BDS via independent certified consultants. A national competency standard for national BDS providers is being developed. There are several online information portals for SMEs, but there is no single-entry portal for the range of BDS services. On the positive side, a number of academic...
institutions, in partnership with private or public institutions, have organised business plan companions across the country. There are also private initiatives, such as an initiative of KADIN Indonesia, the Indonesian Chamber of Commerce, to facilitate capacity building on online marketing and e-commerce for more than 2300 SMEs.

**Productive agglomerations and clusters enhancement**

Both the MoI Strategic Plan 2015-2019 and the Research Centre for Science and Technology (Puspiptek) Strategic Plan 2015-2019 have elements on cluster promotion. Both plans are derived from the National Long-Term Plan 2005-2025. MoI allocated more than IDR 8.9 billion for cluster promotion programmes. Under a 2014 MoI regulation, all industrial sites are to allocate 2% of their land area for SMEs. In 2015, a government regulation stated that all industrial estates should allocate five hectares of their land for SMEs. While there are good initiatives for developing cluster policies in the country, they are limited by a lack of co-ordination among the responsible ministries.

Indonesia scored 84% in the 2014 Foreign Investment Liberalisation (FIL) rate of the Economic Research Institute for ASEAN and East Asia (ERIA), the second lowest score in the region. However, this represented a big increase from 52% in 2011, and the third highest increase since 2011 among AMS. Investment liberalisation in Indonesia is largely autonomous, and progress in this domain reflects the country’s appreciation of the critical role of FDI for total investment in and development of the economy (Intal Jr., 2015).

There are currently 34 science parks in Indonesia – a big increase from 2014, when there were just six – and the government aims to establish 100 technoparks across the country by 2019 to boost productivity and competitiveness. Electronics is one focus sector, and there are also clusters in agroindustry; information and communications technology (ICT); manufacturing; and the marine, medical and pharmacy sectors. One of the biggest parks, in Pulogadung, Jakarta, has 691 SMEs, and an industrial park in Jakarta has reserved 10% of its land area for SMEs. Fiscal and non-fiscal incentives are provided to businesses in the cluster zones. In Special Economic Zones, the government provides generous incentives for pioneer industries, such as corporate tax exemption for up to 25 years. Holistic government programmes for cluster development include partnerships with donors. The Ministry of Youth and Sports provides grants for Sentra Kewirausahaan Pemuda (a kind of cluster for young entrepreneurs). Monitoring is conducted yearly by the different ministries involved. However, there is no independent evaluation of policies on the promotion of industrial clusters. There are some KPIs, such as the number of innovative products produced, the number of economic transactions in the clusters, etc., in addition to the number of SMEs in the clusters.

**Technological innovation**

A National Development Strategic Policy for Science and Technology emphasises the importance of R&D as a driver for Indonesia’s future economic development. National innovation policy, although without specific reference to SMEs, is derived from the 2015-2019 National Development Plan; the responsible institution is the Ministry of Research, Technology and Higher Education, which promotes technological innovation in eight sectors: food, energy, health and medicine, information technology, transportation, defence, advanced materials and maritime. Under this ministry, the Directorate General of Innovation Strengthening is in charge in national innovation programmes, with three directorates: innovation systems, industrial innovation and technology-based entrepreneurship. MoI, meanwhile, focuses on the electrical, transportation machinery
and food processing sectors. Bappenas has a co-ordinating function, inviting relevant institutions for regular co-ordination meetings. Although the responsibilities between agencies are said to be clear, there is no official arbitration mechanism.

Regarding intellectual property (IP) rights, procedures are in place for registration and enforcement, and they are relatively efficient. Among positive changes, it is worth noting the creation in 2015 of an independent government agency, Badan Ekonomi Kreatif (Creative Economy Agency), which oversees 16 creative industry sectors. The Directorate of Intellectual Property launched a copyright e-filing system in 2015. Under the new Patent Law, an online system will be introduced for filing patent applications. Two new laws became effective in 2016: the Trademark Law and the Law on Marks and Geographical Indications.

The government has made a recent push to promote innovation. Its public spending on incubating tech-based businesses has nearly doubled, increasing from IDR 190 billion (USD 14.1 million) in 2015 to IDR 370 billion (USD 27.6 million) in 2016. Yet this amount is still very low given the country's size. Malaysia, for instance, has allocated MYR 200 million (Malaysian ringgit; USD 46 million) to incubate domestic start-ups, while Thailand recently announced that it would create a fund to incubate digital economy start-ups worth USD 147 million. In the budget for 2016, funds were also allocated for the establishment of 45 incubators. Under initiatives like MCSME’s Start-up Incubator Programme (SIP), SMEs can find mentoring support from industry experts, as well as networking and funding opportunities and international exposure. Established across the country and mainly focused on digital start-ups, incubators also provide space and BDS. At the same time, Indonesia enjoys relatively active private-sector participation in the promotion of innovation, with a large number of private-led incubators and accelerators, such as Techbator, Indigo and Kolaborasi.

Environmental policies targeting SMEs

Through its Green Industry Development Plan, Indonesia has developed policies at a high level to support green growth in the private sector. Developed under the Ministry of Industry, the plan does not target SMEs specifically but its provisions are broadly relevant to them nonetheless. The plan is aimed at reducing industrial use of resources and enhancing competitiveness by improving efficiency and environmental performance. It envisions a green shift through investments in better technology and equipment, supported by different approaches. This includes the creation of green industry standards and an associated certification body; a national approach to informing industry about opportunities to become greener and promoting the benefits of a green shift across different sectors; and supporting research and development into green technology and technology transfer. SMEs were consulted through the Indonesian Employer Association, in part to inform them about the existence of the plan.

The plan is broad and introduces a number of different tools that the government is using to support green industry. The fact that it is hosted by the MoI, rather than the Ministry of Environment and Forestry (MoEF), is a strong indication of green mainstreaming. Shifting to green is presented to industry not as a cost of environmental compliance but as an opportunity to grow.

Incentives and instruments for green SMEs

Indonesia has no regulatory instruments in place to encourage the greening of SMEs. However, it does have financial support schemes and incentives across different
ministries. For instance, the Ministry of Finance has a tax and customs incentive for the use of renewable energy. Under the MoEF, the Centre of Forest Development Financing provides soft loans to micro and small enterprises, both directly and through intermediaries. It offers long payback periods (up to 16 years), grace periods and below-market interest rates. Under the MoI’s Green Industry Development Plan, there are programmes to support enterprises in achieving ISO 14001 and other sustainability-related international certifications.

The MoI also provides Green Industry Awards for enterprises (including SMEs) that achieve certain standards of sustainability across the production process, including efficiency in material inputs, waste and emission reduction, and business management. The MoI is also progressively establishing Green Industry Standards for different product groups, from ceramics to milk powder. However, there seems to have been no assessment of how many small enterprises are accessing these incentives or achieving certification. Implementation of green plans at the federal level can be challenging in Indonesia due to the decentralised power structures.

Stimulating entrepreneurship and human capital development (Dimensions 7 and 8)

Indonesia has emphasised the importance of nurturing entrepreneurial mindsets by integrating entrepreneurial learning into its education system. It has also promoted entrepreneurship skills through entrepreneurship programmes that especially target the lower-income population. Its efforts to promote entrepreneurial education and skills throughout the country are reflected in its Dimension 7 score of 4.52.

Indonesia has also developed policies to promote social and inclusive entrepreneurship. Its Dimension 8 score of 3.22 shows that, while a number of policies have been put in place and initiatives are being implemented, further initiatives could be welcome.

Entrepreneurial education

In the education sector, elements of entrepreneurial learning (EL) are clearly incorporated only in Indonesia’s mandatory curriculum for vocational students at secondary levels. There is a required internship programme for vocational students in well-established state-owned and private companies that aims to link the market demand of businesses for skilled labour with vocational learners, but there is no specific government incentive scheme for private service providers that support EL. Non-vocational students do not have a detailed EL curriculum, although EL competency is one of the criteria for school principals in public schools from basic to secondary levels of education. Other initiatives at the secondary level include the expansion of a pilot project to transform public high schools into entrepreneurship-based schools. In 2016, there were 204 pilot high schools spread across the 34 provinces of Indonesia (Irwin, 2016[27]). A work programme by the Ministry of Education and Culture (MoEC) aims gradually to increase the number of entrepreneurship-based high schools, with 1 300 high schools targeted to have EL in 2018 (Atas, 2017[28]).

There is room for improvement at the university level, however. Indonesia still has neither a strategy nor a curriculum to promote EL in universities, although the idea of constructing a nationwide curriculum on entrepreneurship at the university level has been endorsed by the nation’s vice president since 2010 (Wibowo, 2010[29]). What has been set in place to date is an EL module developed by the Higher Education Authority within MoEC in 2013 as a reference for universities that plan to integrate EL in any study
programme. There have also been fragmented initiatives to promote entrepreneurship and EL in universities. For example, the Centre for Entrepreneurship Development and Studies of Universitas Indonesia provides business incubation for students with entrepreneurship interests. Other reputable universities, such as Universitas Gadjah Mada and Institut Teknologi Bandung, have similar business incubation programmes for interested students, while Universitas Brawijaya introduced an entrepreneurship major in 2016 under its Bachelor Degree in Economic and Business programme, strengthening its reputation as a leading university in entrepreneurship education in Indonesia (Widyawati, 2016[30]). With these initial steps to integrate EL into university education, the government now needs a strong and continuous commitment to move forward.

**Entrepreneurial skills**

More than 100 entrepreneurial training sessions are conducted annually by various ministries, such as the Ministry of Research, Technology and Higher Education, the Ministry of Youth and Sport Affairs and the Ministry of Social Affairs, with entrepreneurial skills promotion often integrated into larger programmes for SMEs. One notable initiative is KUBE (*Kelompok Usaha Bersama*), which was implemented in 2007 under the Ministry of Social Affairs as a part of PKH (*Program Keluarga Harapan*), which seeks to empower lower-income groups by providing working capital and entrepreneurial training. This programme creates small groups of 10 households each so that members can collectively manage their respective small businesses and leverage their capacities. The KUBE-PKH programme not only improves the entrepreneurial skills of local micro entrepreneurs and small businesses, but also promotes poverty alleviation by reaching the less developed regions, remote areas and outer islands.

Other initiatives are executed by different ministries and government agencies. In 2016, MCSME established an internship programme for 500 new entrepreneurs in businesses in Bali, West Kalimantan and Central Sulawesi provinces (Hardum, 2016[31]). Around IDR 2.1 billion was allocated to run the programme. Meanwhile, since 2011, the government has implemented the National Movement of Entrepreneurship programme, or *Gerakan Kewirausahaan Nasional* (GKN), to generate more entrepreneurs in Indonesia. GKN, first co-ordinated by MoI, is now run by MCSME. With around 1,500 entrepreneurship coaches in 2017, MCSME aims to provide assistance and mentorship in entrepreneurship to micro entrepreneurs and small businesses across Indonesia (Sofia, 2017[32]).

Initiatives to increase entrepreneurial skills are also conducted by local governments within their autonomous authorities. For example, in 2017 the Jakarta provincial government, DKI Jakarta, launched the One District One Centre Entrepreneurship programme, which provides coherent entrepreneurship assistance and business coaching for micro entrepreneurs across the province, including in Kepulauan Seribu district, in order to reduce the provincial unemployment rate. DKI Jakarta allocated IDR 82 billion for the programme in its 2018 budget plan (Purba, 2017[33]). Within 100 days of its launch, 368 entrepreneurs had joined the programme (Nailufar, 2018[34]). Similarly, since 2015, West Java provincial government has conducted the *Pencetakan Seratus Ribu Wirausaha Baru* programme, which provides intensive mentoring and assistance in starting and running businesses to small business owners and aspiring entrepreneurs in the region. The programme provides specific assistance for different levels of business maturity, from cultivating business ideas to expanding the small business. However, different regions have varying resources and capacities for designing initiatives to nurture entrepreneurship skills among local SMEs and aspiring entrepreneurs, and may not yet be
able to design and implement coherent and relatively advanced programmes like those in Jakarta and West Java province.

Indonesia’s initiatives to increase entrepreneurial skills could be boosted by improved policy design in the development of entrepreneurship programmes, particularly through use of more intensive background studies on the entrepreneurial skills of SMEs. Most government initiatives currently rely only on background studies done by the internal research division in each implementing ministry. It should be noted here that there are variations in the research capacities of such ministries or agencies.

Social entrepreneurship

The regulatory environment for social entrepreneurs has recently evolved under Bappenas, including regulatory assessment for mission-driven start-ups in National Legislation Planning (Prioritas Prolegnas 2015). While there is no official definition of a social enterprise, a definition is implied through the implementation of the KUBE programme. A new law on entrepreneurship is being drafted that may provide a clear definition, with social impact as one of the criteria. Co-operatives could also be considered social enterprises in some cases. The Ministry of Social Affairs (MoSA) is in charge of social enterprises, while the MCSME handles co-operatives.

On the implementation side, the government has been promoting various approaches. The most important, through the KUBE programme and e-Warong (a social protection cash transfer programme), mainly focus on empowering the poor to become socio-economically capable. Other programmes focus on leveraging the private activities of companies and NGOs. Indonesia enjoys a relatively large number of enablers – members of international networks supporting social enterprises, such as UnLtd, Ashoka, Endeavor Indonesia and the INOTEK incubator supported by the British Council. The Ministry of Youth and Sports has conducted a youth social entrepreneurship business-plan competition in co-operation with the University of Gadjah Mada since 2016. In part due to this diversified ecosystem, mainly in large urban areas, Indonesia is singled out by interviewed investors as one of the strongest potential markets for social finance. This perception is also driven by the country’s demographic size, its increasing internet/mobile penetration and its agrarian/maritime potential. According to the Angel Investment Network Indonesia, most social enterprises are active in the agriculture, financial services (fintech), health care, education and fishery sectors. They are mainly young, and generally tap into the seed stage of development (UNDP, 2016[35]).

Inclusive entrepreneurship

Inclusive entrepreneurship in Indonesia is at a relatively early stage of policy development concerning two of the three target groups – women and persons with disabilities (PWD) – but at a more advanced stage concerning the third group, youth.

Although the country has no particular policy on women’s entrepreneurship, a number of policies focus on women’s labour force participation and encouraging entrepreneurship through co-operative activities. The Ministry for Women’s Empowerment and Child Protection is the main body handling the development of women’s entrepreneurship. Most of its activities have been conducted in urban centres, but it has also co-ordinated empowerment programmes in some 20 districts to help women establish co-operatives and it has organised training sessions and business competitions. The private sector plays an active role, especially the Indonesian Women Entrepreneurs Association, which supports a dedicated incubator for women entrepreneurs and conducts training and
mentoring support. The initiatives, which are of relatively low intensity for the scale of Indonesia, mainly focus on entrepreneurs who are just starting out. However, women have benefited from widely available microcredit initiatives across the country.

In relation to youth, Indonesia has developed a comprehensive national strategy, Youth Entrepreneurship Development (2015-2025), which is supported by universities and co-ordinated by the Ministry of Youth and Sports Affairs. Implementation is handled by the Agency for Youth Entrepreneurs Development, which has seven support schemes including training, partnership and financial support. The budget for youth entrepreneurship activities has been increasing and reached IDR 46 billion (USD 3 million) in 2017. Academia plays an active role though initiatives like the College Student Entrepreneurial Programme (IDR 10 billion), and several university incubators host early start-ups. The MCSME also conducted training activities in 2017 for some 500 young school drop-outs focused on improving their entrepreneurial potential. With youth entrepreneurship largely focused on tech and digital start-ups, substantial support is also available from private initiatives conducted by the Association of Young Entrepreneurs, and players such as IYE!, Bank Mandiri or PT Astra International.

The final target group, persons with disabilities, falls under the responsibility of MoSA, which has a mandate for PWD entrepreneurship training and assistance. But although there are scattered PWD support initiatives within MoSA, there is no overarching policy document and only a few initiatives are available. For example, the MCSME conducted an initiative for 35 people in 2014, while the Creative Economy Project has been operational since 2015 through 19 social welfare institutions for PWD. Initiatives run by NGOs, such as BisnisUKM.com, Tiara Handicraft or Klaten, conduct training focused on entrepreneurship for PWD. Yet the dedicated needs of this target group concerning access to finance, accessibility of training locations and access to business acumen skills have not been sufficiently integrated into SME-related policies.

**The way forward**

**Strengthening the institutional, regulatory and operational environment**

Indonesia has taken steps to reform the country’s business environment over recent years, yet more could be done to promote a more strategic and co-ordinated approach to MSME policy and regulatory reform. Moving forward, Indonesia could:

**Institutional framework for SME policy**

- **Consider revising the country’s SME definition.** Currently some opacity exists around the characteristics of the population covered by Indonesia’s SME definition. This has resulted in an inflation of SME numbers and an unmanageably large target group. The formal definition could be extended to include an employment criterion, which is generally an easier data point to collect. A refined SME definition might increase the consistency of its use throughout the country’s civil service.

- **Improve data gathering on SMEs.** Indonesia could consider establishing a shared database of the most relevant indicators on SMEs, collected from across the country and able to be accessed and receive inputs from a broad range of stakeholders.
Legislation, regulation and tax

- **Consider new measures to inculcate good regulatory practices (GRPs).** This could be pursued through the development of training modules and the implementation of a formal requirement to conduct GRPs in the development of major regulations, such as public-private consultation and RIA. Both should be incorporated taking into consideration their impact on SMEs.

- **Streamline company registration.** The large number of licenses and company identification numbers required to run a company is still rather burdensome. Indonesia could conduct a review of requirements that could be eliminated.

Facilitating SME access to finance

Indonesia has invested substantial public funds in MSME financing programmes in recent years, demonstrating considerable public commitment. Moving forward, more could be done to assess the financial performance and additionality of current schemes and to prioritise the development of the institutional, legal and regulatory framework for extending finance. For instance, Indonesia could:

- **Assess the performance of current schemes to stimulate bank lending.** This should be done before committing further public funds. Measures could be considered to enhance the operating performance of existing schemes and to boost their independence and market orientation, for instance by removing the ministerial right to appoint members of the credit guarantee scheme’s governance and supervisory boards. Collateral requirements are almost as high for large enterprises as smaller ones. Therefore measures to improve the legal and institutional environment for the taking of security could be prioritised before the expansion of existing risk-sharing instruments.

- **Develop private equity/business angel regulation.** A strong regulatory framework for the venture capital industry is in place, but there is very little regulatory oversight of private equity and business angel activities.

Enhancing access to market and internationalisation

To better adjust to global trade dynamics, improvements could take place in some areas. Going forward, Indonesia could:

- **Develop support initiatives for SMEs to qualify as an AEO.** Qualifying as an AEO in Indonesia requires advanced management qualities, and SMEs might find difficult to comply with this criterion. Developing mechanisms to leverage SMEs’ management qualities in accordance with the AEO programme’s requirements will not only increase SMEs’ opportunities to enjoy the programme’s benefits but also improve their competitiveness through better management quality. Linking this initiative with national strategies to improve SME quality standards, and collaborating with the national standards agency, will scale up the action to realise more benefits for SMEs and cover a broader area of development.

- **Develop specific measures and strategies to assimilate SMEs to GVCs.** As global trade becomes more integrated, such integration is essential for a big economy like Indonesia. It has equally become increasingly relevant for Indonesia to design strategies specifically aimed at improving SME competitiveness and linkages with larger businesses, both domestic and MNCs, to integrate them into
regional and international value chains. Mechanisms provided in the Foreign Investment Law to encourage local sourcing and partnership should be complemented by rigid and regularly monitored KPIs, for example on how many SMEs are under partnership with MNCs and in what sector or regions, and what kind of technology transfers are being conducted. Specific capacity-building programmes should be developed to help SMEs venture into more complex production networks.

- **Ensure that national programmes reach the entire country.** More rigid guidelines and key indicators should be developed to ensure that national programmes on promoting SME internationalisation reach regions across Indonesia. This is a challenge given the country’s size and archipelagic nature. Several national programmes lack clear outreach mechanisms. For example, the SMEs Go Online programme set targeted numbers of assisted SMEs but did not specify the target for each region. This is particularly important, as SMEs in different regions might possess very different initial capacities. Those in relatively underdeveloped areas or far from the capital might need such initiatives.

*Boosting productivity, innovation and adoption of new technologies*

To improve productivity, innovation and the adoption of new technologies and SME greening, Indonesia could:

*Productivity, technology and innovation*

- **Clarify the roles of institutions that promote productivity.** This is especially important in relation to implementation. The number of agencies involved in policy implementation could create confusion. Clearer understanding of each agency’s role and mandate could improve co-ordination and make programmes more efficient.

- **Focus on growth enterprises.** Although a number of productivity initiatives and support structures focus on micro and small enterprises, few specifically target enterprises enjoying fast growth. By focusing more on these enterprises, Indonesia could benefit from higher growth.

- **Improve productivity monitoring and evaluation systems.** Although monitoring systems exist, few initiatives have gone through independent evaluations, which could help to define instrument-specific weak points and to improve the efficiency and impact of such measures. Monitoring mechanisms could integrate disaggregated indicators focused on SMEs to improve understanding of how specific initiatives have affected SMEs and their subgroups. Monitoring and evaluation could also help with the gathering of statistics, which are often lacking.

- **Further promote innovation.** Although a number of programmes exist, they appear to be mainly focused on collaboration between R&D institutions and the larger companies. Indonesia’s current support structures are rather focused on product innovation research. More could be done to support other types of innovation (e.g. process, marketing and operational), to increase private-sector involvement and to develop mechanisms that help SMEs engage in innovation. One such mechanism could be innovation grants for early stage ideas, supported...
at a later stage by innovation vouchers to help develop an SME proof of concept and business model.

**Environmental policies and SMEs**

- **Further mainstream environmental policies by also targeting SMEs.** The measures included in the Green Industry Development Plan could further be supported by a more detailed list of actions and targets specifically targeting SMEs. By integrating KPIs that also focus on SMEs, it might be possible to ensure that the green development plan is reaching smaller enterprises.

- **Further improve green awareness.** In Indonesia, as in other countries, SMEs are often not aware of the importance of greening and the advantages it could bring. Moreover, they are often unaware of the instruments available. Increasing awareness of the importance of greening and the incentives on offer, especially those targeted at SMEs, might make it possible to improve SME uptake of the instruments available.

- **Improve monitoring and evaluation.** Steps could be taken to strengthen the monitoring and evaluation of policy implementation. Assessing the specific needs of SMEs in relation to greening and translating these needs into indicators might make it easier to monitor whether these needs have been met. The impact of incentives also needs to be monitored and evaluated to ensure that the incentives are accessible to SMEs and being utilised.

**Stimulating entrepreneurship and human capital development**

Indonesia could prioritise the following actions to step up its level of entrepreneurship and human capital development:

**Entrepreneurial education and skills**

- **Develop entrepreneurial education programmes at primary education level.** To move entrepreneurial education forward and develop entrepreneurial attitudes and skills from an early age, Indonesia needs to consider introducing more concrete measures and curriculum on entrepreneurship at primary education level. Nurturing an entrepreneurial mindset is not an overnight process, making it important to instil entrepreneurship elements beginning in primary school. A national curriculum on entrepreneurship will help a large nation like Indonesia to manage and monitor its national entrepreneurial education. Neighbouring AMS like the Philippines and Brunei Darussalam have adopted this idea, integrating entrepreneurial education at the primary as well as the secondary level of education. Indonesia could follow their lead, taking valuable inputs for designing entrepreneurship measures and integrating them into its national education system.

- **Strengthen entrepreneurial education at university level.** Indonesia has mostly focused on fostering entrepreneurial education at secondary level. In the absence of a national agenda on integrating entrepreneurial education into higher education, only a few universities have introduced entrepreneurship programmes. A national programme to introduce an entrepreneurship degree or subjects in public universities would spread entrepreneurial education across the country and encourage universities to follow through with similar efforts.
• **Introduce entrepreneurship programmes nationwide.** Public programmes to develop entrepreneurial skills could support poverty reduction measures in Indonesia. However, programmes are currently fragmented. While there have been several national-level programmes on fostering entrepreneurship, efforts to nurture entrepreneurship and support local economies have mainly relied on autonomous initiatives from local governments. Given the substantial development gaps among regions in Indonesia, collaborative programmes between different regions would strengthen national entrepreneurship initiatives.

**Social and inclusive entrepreneurship**

• **Develop a clear definition or set of criteria for social enterprise.** This could be based on good practice examples in the region. Indonesia’s lack of a legal definition of a social enterprise could be a source of confusion. Although social enterprises are often falsely perceived as charities, they are in fact profit-making businesses, but with a strong social and environmental purpose. A definition could also help with the establishment of a central registry for social enterprises.

• **Develop business skills programmes in partnership with private initiatives.** Indonesia enjoys a number of private initiatives supporting social and inclusive entrepreneurship and could build on this to provide a larger scope of support services that provide business acumen skills to targeted groups. Companies could be supported to establish new business models that capture value and impact. This could help to overcome the lack of compelling capacity-building programmes in Indonesia.

• **Further integrate the needs of the target groups into policies.** As with youth entrepreneurship, the government could consider developing strategies or action plans focused on women’s entrepreneurship or entrepreneurial support for PWDs. Specific needs such as access to finance and specific training facilities as well as means of delivery should be analysed and integrated into the action plans. Consultations with stakeholders could help to identify the best approaches.

**Notes**

1 If in 2016 it had met the current threshold for high-income status, its GNI would amount to current USD 3,294 billion (the fifth highest globally). In 2016 the World Bank’s threshold for high-income status (using the Atlas method) was current USD 12,735.

2 Mining and quarrying accounted for around 12.1% of the country’s GDP in 2000, compared to 6.1% by 2014. Likewise oil and gas manufacturing as a share of total manufacturing decreased from 14.1% in 2000 to 5.9% by 2014 (BPS, 2017).

3 This period is known in Indonesia as the Reformasi.

4 With a population of 261 million people, Indonesia accounts for around 40% of the ASEAN population, and is the fourth most populous country in the world.

5 Measured as the share of its population below the international poverty line (PPP USD 1.90 a day) (World Bank, 2016a).

6 This does not reflect unemployment rates among the working age population as a whole. The ILO-modelled estimate of the unemployment rate in Indonesia is 3.9% for women and 4.5% for men (2017).
7 Indonesia would need to grow at a steady rate of 7% over the next 20 years to join the high-income bracket, yet it is currently projected to demonstrate a GDP growth rate of 5.4% over the next five years (2018-22).

8 The ICOR is a measure of economic efficiency, indicating the increase in investment required to achieve a designated growth rate. In Indonesia’s case, for instance, 5.7% of additional investment would be required to achieve a 1% increase in the GDP growth rate.

9 Indonesia currently ranks 63rd in the Logistics Performance Index (World Bank, 2016[37]), for instance, and lowest on infrastructure indicators.

10 Indonesia ranks 59 out of 63 economies in the OECD’s FDI Restrictiveness Index (2016).

11 As of 31 January 2018: Go-Jek, Traveloka, Tokopedia and Bukalapak.

12 For instance the passage of Presidential Decree No. 13/2018 on beneficial ownership, which requires business entities, such as corporations, foundations and co-operatives, to submit the identities of their beneficial owners to the authorities.

13 It has tried and convicted 119 members of parliament and 17 governors since it was first established in 2002 (as of July 2017).

14 In The Co-operative Movement in Indonesia (1958), Hatta stated that “because the strength of a people economically weak can be brought about only through the co-operative movement, co-operatives are a condition sine qua non as a base for the people’s economy.” Co-operation, he argues, is the only way to eradicate the national “inferiority complex” and “bring the remnant of colonialism from the soul of our nation.”

15 Doing Business data covers Jakarta and Surabaya. In Jakarta, standard procedures to start a business take 22 days and cost on average 10.9% of income per capita, involving 11 procedures. In Surabaya the process costs the same, but takes around 27 days and involves 12 procedures.

16 The effective monthly minimum wage in Yogyakarta, Central Java, Eastern Java and Western Java is IDR 1.5 million for 2018.

17 Both calculated using World Bank official exchange rate (2016 average): USD 1 = IDR 13 308.

18 Data provided by the Co-ordinating Ministry for Economic Affairs.

19 Previous rules were a Presidential Regulation in 2008 and OJK Regulations in 2014.

20 The new Microfinance Law builds on previous laws No.12/POJK.05/2014, No.13/POJK.05/2014 and No.14/POJK.05/2014, and has recently added Regulation No. 22/PMK.05/2017 on Ultra Micro Financing, issued by the Ministry of Finance.

21 OJK regulations passed in 2015 included: Arrangement of Venture Capital Company Business (Reg. No. 35/POJK.05/2015); Licensing and Organisation of Venture Capital Companies (Reg. No. 34/POJK.05/2015); Good Corporate Governance for Venture Capital Companies (Reg. 36/POJK.05/2015); and Direct Inspection of Venture Capital Companies (Reg. 37/POJK.05/2015).


23 Four sets of indicators from the 2017 OECD TFIs are used in the 2018 ASPI: i) Information availability; ii) Fees and charges; iii) Formalities–documents; and iv) Formalities–procedures, with 2 being the highest possible score for each of the indicators. In 2017, Indonesia scored 1.4 for Information Availability; 1.2 for Fees and Charges; 1.1 for Formalities–documents; and 1.3 for Formalities–procedures.

24 The World Customs Organisation (WCO) defines AEO as a party involved in the international movement of goods in whatever function has been validated by, or on behalf of, a national customs administration as complying with the WCO or equivalent supply chain security standards (WCO, 2010[36]). Therefore, customs will trust and expedite procedures for an AEO.
Most R&D in Indonesia is performed by public research organisations, and private sector companies engage in very little R&D.

The ERIA Foreign Investment Liberalisation rate is equal to 60% of the foreign equity liberalisation rate and 40% of the liberalisation rate of other investment restrictions. Please refer to (Intal Jr., 2015) for details on the methodology.

Collateral requirements for large enterprises are around 228.3% the value of the loan, according to Enterprise Survey data (World Bank, 2015).


